rival networks will protect competition.[158] For the reasons set forth below and in the attached Affidavit of Dr. Harris, these unsupported and misleading claims cannot be credited.

A. WorldCom's and MCI's Failure To Identify a Separate Market for Internet Backbone Service Conflicts with the Commission's Market Definition Precedents.

The first step in assessing the competitive impact of the WorldCom/MCI-MCI merger on Internet services is defining the relevant product and geographic markets. Both the DOJ, in its Antitrust Guidelines,[159] and the Commission, in the *Bell Atlantic NYNEX Order,*[160] focus their market analysis on the question of substitutability. The Commission has stated that "'market definition focuses solely on demand substitution factors, *i.e.,* possible consumer responses.'"[161] One service is a demand substitute for another if, when all providers of the first service raise their prices, customers will switch to the second, lower-priced service.[162] If two services are not demand substitutes, they will not be found to be in the same market. Consistent with these principles and with the Internet market distinctions adopted in the Commission's *Digital Tornado* study,[163]

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[158] *See generally* Joint Reply.

[159] *Merger Guidelines*, Section 1.0.

[160] *Bell Atlantic/NYNEX Order,* ¶ 50.

[161] *Id.*

[162] *Id.*

[163] *Digital Tornado: The Internet and Telecommunications Policy*, Mar. 1997, at 10-12 (OPP Working Paper Series, 29).

GTE and numerous other petitioners and commenters identified a separate Internet backbone service product market relevant to these proceedings.

Only WorldCom and MCI dispute this analysis. First, they "vigorously disagree with the suggestion that there is a separate 'Internet backbone' market" because, they contend, the transmission facilities that underlie Internet services and other circuit-switched and packet-switched services are fungible.[164] They further suggest in connection with their own attempted market share analysis that, even if there is a distinct Internet services market, it encompasses virtually all Internet-related offerings from backbone transmission to access services to content. Notably, however, even their economic experts Carlton and Sider do not support these claims.[165]

Internet backbone services involve "the transporting and routing of packets between and among ISPs . . . and other regional and national backbone networks."[166] Backbone service providers interconnect with each other for the exchange of traffic under so-called "peering" arrangements and provide their services to other backbones and to ISPs. On this basis, Dr. Harris concludes that the "backbone service market can be narrowly defined as a product market because there do not appear to be good

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[164] Joint Reply at 69-70.

[165] Indeed, in their affidavit, Carlton and Sider use the term "backbone provider" in a context that is wholly consistent with GTE's analysis herein. *See* Carlton/Sider Declaration at 26-28.

[166] Harris Internet Affidavit at 7. The *Digital Tornado* study similarly notes that: "Backbone providers, such as MCI, UUNet, and Sprint, route traffic between ISPs, and interconnect with other backbone providers." *Digital Tornado* at 12. Information service providers, or "ISPs", on the other hand, "connect . . . end users to Internet backbone networks." *Id.*

demand substitutes for . . . obtain[ing] national Internet access . . . if a hypothetical backbone service monopolist were to raise its connection price above competitive levels."[167]

Contrary to WorldCom's and MCI's arguments, the potential availability of other transmission facilities that might be used to provide backbone service does not expand this backbone "market" to include all such facilities. As Dr. Harris explains, substitutability is determined from the *buyer's* perspective, *i.e.*, a product will be deemed a substitute for another product only if a potential customer perceives it to have the same utility as the final product.[168] This is consistent with both the Commission's and the DOJ's market definition requirements. Although transmission facilities are necessary inputs to a backbone service, standing alone they may not simply be substituted for backbone service.

Even WorldCom and MCI acknowledge that alternative communications transmission facilities may not be utilized to provide backbone services until they are properly configured into an Internet backbone network using the necessary conditioning and routing equipment.[169] Moreover, an entity constructing such a network would not realistically be able to sell "backbone" services unless it was assured of the ability to interchange traffic through interconnection arrangements with other backbone operators, including WorldCom and MCI. It follows that the availability of other

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[167] Harris Internet Affidavit at 7.

[168] *Id.* at 6.

[169] Joint Reply at 69.

transmission services and facilities is merely one of several factors that affect the potential for new providers to enter the Internet backbone market, not the definition of the market itself.[170]

In a separate, collateral attack on the Internet backbone market definition, WorldCom and MCI do concede, at least for purposes of argument, that there may exist some Internet market separate from the entire telecommunications marketplace. But, they suggest that their share of that market would be only approximately 20 percent, as opposed to the almost 50 percent or more share calculated by GTE and other parties.[171] They base this claim on an industry report by Frost & Sullivan that totals virtually all Internet-related industry revenues without discriminating among the various Internet product groups.

Thus, WorldCom and MCI apparently would include revenues from ISPs such as the AOL and Microsoft Network online services as well as those of smaller ISPs and other Internet industry players in their product market definition.[172] However, as noted above, ISPs provide "Internet connectivity to end-use customers through dial up or dedicated connections,"[173] and typically connect their customers to Internet backbones,

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[170] Thus, WorldCom and MCI are "confusing the issue of barriers to entry with the issue of product definition." Harris Internet Affidavit at 7. *See* Section IV.D, *infra.* While relevant to an assessment of the competitive impact of the proposed merger, the existence or absence of barriers to entry does not change the definition of an otherwise distinct product market.

[171] *Compare* Joint Reply at 76 *with* GTE Response at 6.

[172] *See* Harris Internet Affidavit at 15-16.

[173] *Id.* at 9.

which then transport and route the customer's data.[174] Plainly, providing end users with such connectivity to a backbone is a different product than transporting and routing traffic among ISPs over a backbone.[175]

Further, online services such as AOL and Prodigy and website hosts such as Yahoo! and CNN.com provide substantial proprietary content for which they also earn revenues. Such content likewise is obviously not a substitutable product for backbone service.[176] Given that neither these nor any other services are "adequate substitutes . . . that would enable backbone consumers to counteract price increases foisted upon them by a backbone service monopolist,"[177] Internet backbone service must be considered a separate relevant product market for purposes of this competitive analysis.

B. WorldCom and MCI Have Failed To Address the Relevant Geographic Market for Internet Backbone Service.

WorldCom and MCI do not even discuss the relevant geographic markets for Internet-related services. Nonetheless, Dr. Harris explains that "[t]he geographic market for backbone service is limited to the area in which it is cost-effective for ISPs to

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[174] *Id.*

[175] *Id.* at 9-10. The fact that some ISPs may be vertically integrated and provide backbone services to themselves and other ISPs does not undermine this distinction between the ISP and backbone markets.

[176] *See id.* at 10.

[177] *Id.* at 7, n.8.

lease or buy transport facilities connecting them to a regional or national backbone."[178] Thus, if an ISP is unsatisfied with the price charged by backbone networks in its area, but the cost of leasing or buying the fiber needed to interconnect with a more distant backbone network imposes a significant additional expense, the local and distant networks would be in different geographic markets.[179]

GTE assumes that the geographic market for backbone services is national because "there are a number of national backbone service providers that offer interconnection in major metropolitan areas."[180] This is a conservative assumption because "there are probably some geographic areas where the separate MCI/WorldCom backbones provide a much higher share of backbone service than would be indicated by their average nationwide share."[181] In these areas, the costs of connecting to more distant networks would impose significant additional costs.

C. WorldCom and MCI Have Failed To Identify the Most Significant Participants in the Internet Backbone Market As Well As To Reveal the Merged Entity's Dominant Position.

1. WorldCom and MCI Misidentify the Relevant Backbone Market Participants.

Having failed to define correctly the relevant Internet-related markets, it is not surprising that WorldCom and MCI likewise erroneously identify the major market participants, albeit by implication. As noted above, the Applicants' putative market

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[178] *Id.* at 8.

[179] *Id.*

[180] *Id.* at 8-9.

share analysis relies on a report that aggregates revenues from the entire cross-section of Internet businesses, including ISPs, content providers, and backbone operations. Because they do not provide substitutes for backbone services, the many ISPs and content providers identified by Frost & Sullivan cannot be considered participants in the backbone market. WorldCom and MCI have, therefore, failed to carry their burden on this *Bell Atlantic/NYNEX* requirement as well.

In fact, based on available information, there are only nine Internet backbone providers with more than one percent market share: MCI, Sprint, WorldCom (UUNet, CIS, ANS, GridNet, and Verio), AGIS, BBN, DIGEX, CRL, GOODNET, and iStar.[182] These networks represent approximately 88 percent of the backbone market measured by number of small ISP connections.[183] Of these "major" participants, MCI, WorldCom and Sprint are by far the largest, with 29.36 percent, 19.98 percent, and 22.57 percent, respectively. A number of small backbone providers comprise the remaining 12 percent.[184] Notably, large ISPs such as AOL and CompuServe, who were previously vertically integrated into the backbone market, have now exited that market and sold their networks to WorldCom.

(...Continued)

[181] *Id.*

[182] *Id.* at 19.

[183] *Id.*

[184] *Id.*

Potential new entrants include AT&T and the Bell operating companies.[185] The latter, however, will require significant regulatory relief to enter this market, and the prospects for such relief in the near term remain uncertain. Because of the existence of the substantial entry barriers discussed below, the concentration in the backbone market resulting from the merger would not likely be relieved in the near future.

2. The Merged Entity Will Be the Dominant Backbone Provider.

Based upon the foregoing marketplace analysis, GTE and a host of other petitioners and commenters calculated that the proposed merger would create a dominant backbone provider with approximately a 50 percent or greater market share.[186] GTE derived its estimate from the only publicly available source of relevant data, published counts of the number of ISP connections to the major backbones. Although these data are not ideal, they are the best that can be obtained at this time.

WorldCom and MCI, on the other hand, argue that revenues provide a better measure of market share and that, by such a standard, the merged company would control only about 20 percent of what they deem to be the relevant market.[187] They computed their market share numbers by first estimating total revenues for the Internet

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[185] The Commission requires applicants to identify potential new entrants. See *Bell Atlantic/NYNEX Order* at 20000, 20019-35.

[186] *See* GTE Response; CUIISP Reply at 1-3; CWA Reply at 5-8; Consumer Project on Technology Reply at 2; Simply Internet Response at 2; Bell Atlantic Petition at 4-6; CWA Comments at 5-7; ICP/COTM Petition at 2, 8-9; Simply Internet Petition; Telstra Comments at 9.

[187] Joint Reply at 76.

industry in 1997 by "doubling the total 1996 Internet industry revenue figure of $2.3 billion taken from the Frost & Sullivan study."[188] They then applied "the 1997 estimated Internet revenue of WorldCom and MCI to that base figure."[189]

Importantly, however, revenues for the relevant market – the Internet backbone market – are not separately available. As revealed above, the methodology adopted by WorldCom and MCI unreasonably lumps revenues from the relevant backbone services market together with revenues from other Internet-related markets, such as the Internet access, Internet advertising, and host-based services markets.[190] For example, the Frost & Sullivan study reveals that "48.3% of their forecasted 1997 total Internet revenue is associated with 'on-line' services, such as AOL, CompuServe, and MSN."[191] Because WorldCom and MCI, as backbone providers, and AOL, CompuServe, and MSN, as on-line services, for the most part provide substantially different, non-substitutable services to their respective customers, it is inappropriate to include all of the latters' revenues in the revenue estimate for the relevant backbone market.[192]

In fact, as Dr. Harris observes, "if revenues for ISP services (including on-line services) were deducted from the numerator and denominator of MCI/WorldCom's analysis [Dr. Harris] would be surprised if MCI/WorldCom's resulting backbone market

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[188] *Id.* at 76-77, n.124.

[189] *Id.*

[190] Harris Internet Affidavit at 15-16.

[191] *Id.* at 16.

[192] *Id.*

share was not in the 40-50 percent range."[193] Significantly, this figure would be consistent with the earlier market share estimates provided by GTE and other petitioners and commenters.[194]

The market share figures derived by Dr. Harris are based on the only relevant data now in the public domain – the number of small ISPs' links to backbone operators published in BoardWatch magazine.[195] Controlling for variations in the relative size of ISPs as well as the presence of ISPs connected to multiple backbones, Dr. Harris

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[193] *Id.* Indeed, this figure may understate the merged entity's market position because (1) vertically integrated backbones/ISPs tend to self-supply backbone services and (2) backbones typically offer wholesale discounts to the largest ISPs (such as under WorldCom's long-term contracts with AOL and MSN). These practices may depress the relevant revenue totals. *Id.* at 15.

[194] It should not be surprising that the merged entity would control so much of the backbone market after the proposed merger. WorldCom has been buying up the Internet backbone at an alarming pace over the past several years. The company now owns three national backbones outright, UUNet, CNS, and ANS. Harris Internet Affidavit at 12. It owns a majority of another major backbone, GridNet, and has an interest in a fifth, Verio. *Id.* Its acquisitions, mergers, and strategic alliances have also allowed the company to integrate vertically into Internet-related markets both domestically and internationally. *Id.* at 11-13 For example, WorldCom also has long-term contracts with two of the largest ISPs in the world, AOL and the Microsoft Network, to provide backbone and other network services. *Id.* at 11-12. The purchase of WillTel gave WorldCom control of an extensive telecommunications network as well. *Id.* at 10.

[195] *Id.* at 17. Another advantage of measuring market share by analyzing the percent of total ISP connections is that it reflects to some extent the relative value of a backbone in terms of important network externalities. The significance of accounting for network externalities in the backbone market cannot be overstated. As described by Dr. Harris:

> Not only do the actual existence of network externalities create a barrier to entry, but the expectations generated by the presence of network externalities enhances the barrier because it affects consumers behavior in choosing a particular backbone seller. Michael Katz and Carl Shapiro explained . . . "[that] if consumers expect a seller to be dominant, then consumers will be willing to pay more for the firms product and it will, in fact be dominant." *Id.* at 24.

concludes that the merged entity will link to 49.34 percent of all small ISPs and 46.88 percent of the total bandwidth devoted to small ISP connections.[196] These figures are likewise consistent with other market share submissions in this proceeding.

Inclusion of connections to large ISPs would likely drive the merged entity's market share even higher. Large ISPs often are vertically integrated into the backbone market, or have long-term contracts with separate backbone providers.[197] For example, UUNet supplies a substantial portion of backbone capacity used by it as a vertically integrated ISP, and WorldCom has long-term contracts with both AOL and the Microsoft Network, which together account for 50 percent of the market for household customers.[198] Moreover, UUNet is among the largest providers of backbone services directly to business customers.[199] Thus, it is improbable that the addition of market share figures for large ISPs and companies would reduce the above percentages.

D. WorldCom and MCI Have Failed To Address the Substantial Barriers To Entry in the Internet Backbone Market.

The foregoing establishes that a merged WorldCom/MCI-MCI would enjoy a dominant position in the market for Internet backbone and exchange services. It is equally true that the merged entity would not be precluded from exercising the market power arising from that status to the detriment of its rivals and, ultimately, consumers.

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[196] *Id.* at 21.

[197] *Id.* at 19-20.

[198] *Id.* at 20.

[199] *Id.* at 19-20.

This is so because, given the marked interdependence of the industry participants, "[o]nce dominance or market power is achieved in a networked industry, the externalities that helped create the market power make it extremely difficult for new entrants to dislodge the dominant player."[200] Here, the externality value attendant to the merged company's concentration of ISP customer connections confirms this point. As John Sidgmore of WorldCom/UUNet explained: "Having a big network is a huge barrier to entry for competitors."[201]

This consideration disposes of WorldCom's and MCI's simplistic assertions that they will be constrained from exercising market power with respect to backbone services because anyone can easily obtain additional capacity, either through technological upgrades to existing networks or from alternative sources of the transmission and other services necessary to configure their own backbone.[202]

First, any new, alternative backbone would still require access to the merged entity's customers via traffic interchange arrangements with that dominant network. Without access to the end users, web sites, and ISPs that comprise that system, the customers of other backbones will be denied access to most of the Internet. Thus, new entrants would be in the same vulnerable position as existing rival backbones, equally dependent upon interconnection arrangements which the merged entity would lack any

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[200] *Id.* at 23.

[201] Rajiv Chandrasekaran, "Making UUNet Into a Very Big Deal; With His Agreement With CompuServe and AOL, CEO John Sidgmore Takes It to Another Level," *Wash. Post*, F12, Sept. 29, 1997.

[202] Joint Reply at 73.

incentive to facilitate. Second, technical advances that may increase the capacity of existing facilities will not alter the relative size of the merged entity's network because such advances will likely increase capacity for all players by a proportionate amount. As noted by one industry observer, even before taking such advances into account, after the merger, WorldCom and MCI will have "more bandwidth than God."[203]

The barriers to entry created by these network externalities will be reinforced by customer expectations. Customer recognition of the "value" of the merged entity's backbone with its dominant share of customer connections will be translated into a preference for connection to that backbone.[204] Even other backbone operators will prefer direct connection to the dominant backbone rather than risking service degradation caused by transiting other backbones suffering from the exercise of the merged entity's market power.

Additional significant barriers to entry are likely to arise from the increasing integration of Internet backbone service providers with facilities-based carriers.[205] The significance of telecommunications costs to any backbone network suggests that the benefits attendant to ownership of underlying transmission facilities will confer substantial competitive advantages on integrated networks.[206] At the same time, the

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[203] K. Gerwig, *WorldCom: More Bandwidth than God*, Internet Week, Sept. 5, 1997 (quoting Dwight Gibbs, Chief Technology Officer of the Motley Fool).

[204] Harris Internet Affidavit at 24.

[205] *Id.* at 25.

[206] *Id.*

need to invest in facilities construction to serve those locations not reached by the major alternative networks or services will exacerbate these advantages and further deter entry.[207]

Another barrier will grow out of the merged entity's control over a number of the major NAPs, where smaller and particularly new entrants would typically seek interconnection with larger backbones because they lack the traffic levels necessary to support private interchange arrangements. Specifically, WorldCom's ownership of two of the key public network access points will buttress the merged entity's dominant position in the Internet backbone market.[208] GTE has previously demonstrated that this will permit WorldCom and MCI to exercise a measure of control even over traffic that does not transit their network.[209] In response, the Applicants argue that the recent proliferation of NAPs makes such behavior impossible.[210] These new NAPs, however, are not adequate demand substitutes for the existing key interchange facilities or for private interconnection arrangements.

Perhaps most importantly, a NAP is only valuable to a backbone or ISP if many other backbones and ISPs "present" themselves at that interconnection point. Otherwise, the NAP serves no purpose. Because there is no evidence that WorldCom and MCI, much less any other significant backbone operators, are making their

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[207] *Id.*

[208] *Id.* at 24.

[209] GTE Response at 8.

[210] Joint Reply at 86-88.

networks available for traffic interchange at the new locations in any numbers, the availability of these NAPs has not and will not diminish WorldCom's ability to wield power over Internet exchange services.

As a result, the existing congestion at the key NAPs can be exploited by WorldCom and MCI. To the extent they refuse to upgrade and expand facilities in their NAPs to meet new traffic demands, their rivals will be forced to invest additional resources to secure quality interconnections.[211] The cost increases attendant to such investments will constitute a substantial barrier to entry. For all of these reasons, it is highly unlikely, even given the tremendous continuing expansion in Internet traffic levels, that new entry will materially circumscribe the exercise of market power by the merged entity.

E. WorldCom and MCI Have Failed To Rebut Evidence of the Merger's Serious Competitive Consequences for Internet Backbone Providers and Consumers.

The merged entity's market power in the Internet backbone and exchange markets will give WorldCom and MCI the incentive and the ability to undermine competition. The key to the successful operation of the Internet is efficient, high-capacity interconnection among the principal national backbone networks.[212] Currently, these networks interconnect through bilateral agreements at private interchanges and the public network access points. Because each backbone provider must be able to offer its customers access to the entire Internet, and no one provider now commands

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[211] Harris Internet Affidavit at 24.

[212] Response of GTE at 4.

disproportionately more connections to Internet destinations, each provider has a strong economic incentive to cooperate with all other backbone providers to insure high-quality and high-capacity interconnection. This interdependence means that all networks must offer equivalent interconnection or suffer market share loss when their customers do not receive ubiquitous access to the entire Internet.

The merger of two of the largest backbone networks would destroy this competitive balance, creating an Internet Goliath that dwarfs even its closest competitors. The size and power of the WorldCom/MCI network will mean that the benefits the merged entity will receive from interconnecting with rival backbones will be far less than the benefits its rivals receive from interconnecting with it.[213] As a result, the merged entity's "incentives will be to mesh its own separate backbone networks as efficiently as possible, and interconnect with other players only in a manner which promotes its interests without regard for the other companies."[214] The emergence of such a dominant provider at this time raises enhanced concerns because the Internet is at a "critical phase"[215] in its commercial development and the exercise of market power by such a entity could distort this development in ways that are "particularly harmful."[216]

Analysis of the merger under the DOJ's HHI methodology is instructive. The Internet backbone market is already "highly concentrated," at least in terms of the

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[213] Harris Internet Affidavit at 2.

[214] *Id.* at 26.

[215] *Id.* at 3.

[216] *Id.* at 25-26.

number of ISP connections. The pre-merger HHI for the backbone services market is 1837 under the connections-based market share methodology, and it remains a not insubstantial 1394 under the bandwidth-adjusted methodology.[217] Most importantly, post-merger HHI figures increase dramatically under both methodologies and significantly exceed the DOJ's 1800 threshold for classifying a market as highly concentrated. The post-merger HHI would be 3010 under the connections-based methodology and 2492 under the bandwidth-based methodology.[218] Therefore, the change in HHI would be 1173. under the connections-based methodology and 1098 under the bandwidth-based methodology.[219]

It is important to understand, however, that these HHI indices probably understate the vulnerability of the backbone market to the exercise of market power by WorldCom/MCI. As explained by Dr. Harris:

> In the case where competing providers of a networked service are dependent upon each other to create value, concentration can have a direct adverse effect on both consumers (in this case ISPs and Internet end users) as well as competitors (other backbone service providers). For this reason, the same amount of market share concentration in the Internet backbone industry could be orders of magnitude more harmful for overall welfare than it would be in a non-network based industry.[220]

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[217] *Id.* at 22.

[218] *Id.*

[219] *Id.* at 22.

[220] *Id.*

With this market power, the merged entity will have the ability and incentive to degrade the quality and increase the costs of rival backbone providers' service. Specifically, the merged entity will be able to use its dominance in the backbone market to exercise market power by charging monopolistic interconnection and usage rates, degrading interconnections, and imposing its own standards on other players which might lead to long-term structural advantages vis-à-vis other competitors.[221] These actions will cause the service quality of rival backbones to deteriorate and their costs to increase but, because of the merged entity's dominant network, they would lack competitive alternatives.

Additionally, as described above, WorldCom's control of two key NAPs will exacerbate the competitive impact of a WorldCom/MCI-MCI combination. In order to further its dominance in the backbone services market, WorldCom/MCI could exploit its influence in the Internet exchange service market by making it difficult for rival backbones and ISPs to interconnect with each other at NAPs. The merged entity could accomplish this goal through various actions, such as slowly rolling out the necessary interconnection equipment, or refusing to alleviate congestion at the NAPs where its competitors interconnect, while ensuring high-quality, high-speed interconnection for its own backbone network and its client ISPs.[222] This tactic would be readily available in

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[221] *Id.* at 26.

[222] *Id.* at 2-3.

the current environment of geometric traffic growth and increasing congestion on the Internet.[223]

These actions would tip the competitive balance in the merged entity's favor. As costs rise and quality plummets, rival backbones will lose customers who will flock to the cheaper and higher quality "on-net" services of the merged entity. Dr. Harris points out that MCI's and WorldCom's long term contracts with AOL and MSN, the largest ISPs serving the consumer markets, render it unlikely that they would switch backbones, and their customers would face serious disincentives to changing ISPs. In contrast, many other backbones' customers especially content provides, could more easily migrate to WorldCom/MCI.[224] Furthermore, as explained by Dr. Harris, "[o]nce dominance or market power is achieved in a networked industry, the network externalities that helped create the market power make it extremely difficult for new entrants to dislodge the dominant player."[225]

The merged entity's dominant position will ultimately work to the detriment of consumers. Without real competition, and with huge barriers to new entry in the critical backbone market, prices across all Internet-related markets will rise and output will fall. Consumers will pay more for fewer choices, and the public will suffer.

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[223] *See* at 4.

[224] *Id.* at 27-28.

[225] *Id.* at 23.

V. WORLDCOM AND MCI HAVE NOT DISCHARGED THEIR OBLIGATION UNDER *BELL ATLANTIC/NYNEX* TO DEMONSTRATE THE EFFECTS OF THE MERGER ON COMPETITION AND THE PUBLIC INTEREST IN THE LOCAL EXCHANGE AND EXCHANGE ACCESS MARKET.

In its Petition, GTE explained that the Applicants had supplied no factual basis for evaluating their claims that the merged company would be an aggressive local exchange competitor: "the proposed merger of WorldCom and MCI simply combines two existing competitors or potential entrants into a single entity, with no evidence that there will be any measurable increase in competition or substantial benefits to end users."[226] GTE further noted that WorldCom and MCI have substantial overlaps in their existing and planned local exchange facilities and that the asserted synergies and efficiencies appeared simply to reflect cost savings from diminished competition.[227] GTE therefore cautioned that "a merger involving a significant market participant and another major local exchange player at this early stage of competition requires far more information than WorldCom and MCI have provided."[228]

The Joint Reply provides no further basis for the Commission and interested parties to ascertain the competitive and public interest effects of the proposed merger. It does not even attempt to comply with the *Bell Atlantic/NYNEX* framework for analyzing competitive impacts and utterly fails to substantiate the claimed pro-

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[226] GTE Petition at 43.

[227] As discussed in the next section of these Comments, GTE's initial assessment that the claimed synergies result largely from "revenue enhancements" due to lessened competition has been echoed by Wall Street analysts.

[228] GTE Petition at 44-45.

competitive benefits. Consequently, as discussed below and in the next section, the Commission and the public are in no better position today to assess the significance of the proposed merger for local exchange competition than they were when WorldCom and MCI filed their facially deficient applications.

A. The Applicants Fail To Identify the Relevant Product Markets or To Discuss the Impact of the Merger on Specific Classes of Customers.

The Joint Reply is devoid of information regarding the relevant local exchange product markets or the potentially disparate impact of the merger on different classes of customers. For example, the Applicants have neglected to provide information regarding which customer groups they currently service, and which groups they plan to serve following the merger. This failure is particularly troubling given MCI's recent determination that it would discontinue reselling local service to residential customers and instead focus on providing facilities-based local service to business customers.[229] Against this background, the Applicants' cautiously worded and heavily qualified commitments to provide local residential service certainly cannot be given full faith and credit, at least in the absence of verifiable supporting documentation evidencing firm plans to use the purported synergies generated by the merger to serve local residential customers.[230]

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[229] In a recent speech, MCI's President, Timothy Price, said, "Spending money on resale . . . is not an investment. It's throwing money down a rat-hole." Remarks of Timothy F. Price at the National Press Club, at 4 (Jan. 22, 1998). Mr. Price further indicated that MCI may not provide additional residential services for some time to come. *Id.*

[230] *See* Letter from Bernard Ebbers of WorldCom and Bert Roberts of MCI to FCC

(Continued...)

B. The Applicants Implicitly Define the Relevant Geographic Market in a Manner That Is Inconsistent with Commission Precedent and Unreasonably Narrow.

Instead of expressly addressing the *Bell Atlantic/NYNEX* requirement that they define the relevant geographic market, WorldCom and MCI simply assert that "there is no 'overlap' in the sense of duplicate or redundant facilities."[231] By way of further explanation, they state that "[f]requently, [their] networks in the same city do not reach the same customers, do not serve the same buildings, do not traverse the same streets or are not configured in a similar manner."[232] This network versus network or building versus building approach is inconsistent with Commission precedent and irrelevant to whether MCI and WorldCom serve "overlapping" markets.

In *Bell Atlantic/NYNEX*, the Commission concluded that each point-to-point market constitutes a geographic market and that such market can be aggregated in areas where all consumers "will likely face the same competitive alternatives for a product."[233] Notably, the Applicants do not dispute that they both have facilities in at least 26 of the same cities. However, they simply assert that these facilities are not redundant, without verifying this claim through the provision of maps, identification of buildings served, or submission of other relevant data. Nor do they indicate whether

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(...Continued)
Chairman William Kennard (dated Jan. 26, 1998).

[231] Joint Reply at 16.

[232] Joint Reply at 16.

[233] *Bell Atlantic/NYNEX Order*, ¶ 54.

they could compete for the same customers regardless of the fact that their facilities may not be precisely collocated. Clearly, though, they must believe that such competition is possible, or they could not claim that they will realize such substantial cost savings by eliminating "duplicate" investment.[234]

The Applicants cannot have it both ways. If their facilities in overlap markets permit them to compete with each other, then their proposed geographic market definition is unduly narrow because it would prevent the Commission from considering whether the consolidation is anticompetitive. On the other hand, if their facilities do not permit them to compete for the same customers, then their planned reduction in investment necessarily will diminish competition because the combined company will not be able to compete for the business of customers served by the foregone facilities. Once again, the Applicants must provide considerably more data before a reasoned assessment under *Bell Atlantic/NYNEX* can be made.

C. Applicants Fail To Satisfy Their Burden of Identifying the Most Significant Market Participants and Demonstrating That the Merger Would Not Adversely Affect the Development of Local Exchange Competition.

WorldCom and MCI make only a brief attempt to identify competitors in the local exchange and exchange access markets, stating that "[CLECs] throughout the country are all potential competitors in local exchange markets. . . . Moreover, other potential competitors include electric and gas utilities, wireless, other interexchange carriers, independent telephone carriers, construction companies, cable companies and out-of-

[234] Joint Reply at 16; WorldCom, Inc. Amendment No. 3 to Form S-4 Registration under the Securities Act of 1933, at 42.

region ILECs."[235] Such assertions, however, are insufficient to satisfy the Applicants' burden of identifying most significant competitors.

Plainly, the incumbent LEC in each of the overlap markets is a significant participant, as is MCI,[236] and WorldCom as well, given its acquisition of Brooks Fiber and MFS. The Applicants have not disclosed, however, whether any other actual or potential competitors exist in each of the overlap markets. Nor have they disclosed their pre-merger plans to compete, which would indicate whether the two companies, but for the merger, would have been rivals. Such information, which would be contained in the Applicants' Hart-Scott-Rodino filings, must be disclosed and analyzed before the Commission can determine whether the merger might impede local exchange competition.

D. There Is No Basis for Ascertaining the Competitive Impact of the Proposed Merger in the Local Exchange Market.

In short, the applications and Joint Reply provide no reliable basis for assessing the true impact of the proposed merger on local exchange and exchange access competition. The combined entity may truly be a strengthened, more aggressive competitor, or it may simply benefit from less competitive pressure by virtue of the elimination of a most significant competitor from the marketplace. It may truly bring competition to residential consumers, or it may simply focus on the lucrative large

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[235] Joint Reply at 17. Although Applicants did argue that the incumbent local exchange carrier is the most significant competitor in any local exchange market, they also must identify others that have or would have the ability to present significant competition.

[236] BT/MCI Order at ¶ 61-68.

business sub-market. And, as discussed in the next section, it may truly recognize billions of dollars in efficiencies and synergies, or it may simply terminate planned investments, with the attendant losses in competition, employment, and consumer benefits. The Applicants have been given two tries to demonstrate that their version of events will occur and that the merger raises no concerns under applicable Commission standards, but they have failed to do so. Under the applicable standards their applications must be dismissed or, at a minimum, set for hearing.

VI. THE APPLICANTS HAVE FAILED TO CARRY THEIR BURDEN OF DEMONSTRATING THAT THE MERGER IS IN THE PUBLIC INTEREST.

A. The *Bell Atlantic/NYNEX* Standard Requires Applicants To Verify Efficiencies and Synergies and Show That Any Benefits Would Not Arise "But For" the Merger.

Under the *Bell Atlantic/NYNEX* standard, applicants must show that "the transaction on balance will enhance and promote, rather than eliminate or retard, competition."[237] Pro-competitive benefits "include any efficiencies arising from the transaction if such efficiencies are achievable only as a result of the merger, are sufficiently likely and verifiable, and are not the result of anticompetitive reductions in output or increases in price."[238] This showing is an essential ingredient, one that permits the Commission to quantify what would otherwise be amorphous claims of

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[237] *Bell Atlantic/NYNEX Order,* ¶ 157.

[238] *Id.*